

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
FINANCIAL STATEMENTS  
JUNE 30, 2005

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## Independent Auditors' Report

To the Management  
Drinking Water Revolving Loan Fund  
State of Delaware

We have audited the accompanying financial statements of Drinking Water Revolving Loan Fund (the Fund) of the State of Delaware, as of and for the years ended June 30, 2005 and 2004. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Fund and are not intended to present the financial position of the State of Delaware, and the results of its operations in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Fund, as of June 30, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated January 26, 2006, on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain laws, regulations, contracts and grant agreements. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the

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## Independent Auditors' Report (Cont'd.)

internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information on pages 27 through 30 is presented for purposes of additional analysis and is a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

*McBride, Shogan & Co*

Wilmington, Delaware  
January 26, 2006

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
JUNE 30, 2005

The State of Delaware Drinking Water Revolving Loan Fund (the Fund) established through Chapter 79, Title 29, Subsection 15 of the Delaware Code, provides financial assistance to eligible public water systems in Delaware for the planning, design and construction of drinking water facilities as well as loans for land acquisition for source water protection purposes. The Fund is funded through federal capitalization grants as established under Section 1452 of the Safe Drinking Water Act. The Act requires the State of Delaware to provide matching funds equal to 20 percent of federal funds received.

The Fund is administered by the State of Delaware, Department of Health and Social Services (DHSS), Division of Public Health (DPH) under the supervision of the Governor's Cabinet Committee on State Planning Issues. DPH's primary activities include making loans, providing direct assistance and managing the Fund to meet the objectives of the Safe Drinking Water Act.

The Fund is made up of five sub-funds, each of which is considered a separate accounting entity. The primary activity of the Loan Fund is the issuance of loans. The four Set-aside Sub-Funds are used to account for the proceeds of specific grant revenues that are legally restricted to expenditures for specific purposes.

The Fund's activities are accounted for as a distinct operating unit within the DPH. Accordingly, the financial statements of the Fund are intended to present the financial position and the results of operations of only that portion of the funds of the State of Delaware that is attributable to the transactions of the Fund.

The Fund is accounted for as an enterprise fund. The accrual basis of accounting is utilized in enterprise funds. Revenue is recognized when earned and expenses are recognized when the liability is incurred.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS (Cont'd.)  
JUNE 30, 2005

This section of the Fund's annual financial report presents management's discussion and analysis of the Fund's financial performance for the fiscal year ended June 30, 2005. All amounts in management's discussion and analysis are in thousands of dollars unless otherwise noted. Please read it in conjunction with the Fund's financial statements, which follow this section.

Financial Highlights

The Fund realized a change in net assets of \$5.7 million in fiscal year 2005, which represents an decrease of 42.4% from the change in net assets of \$9.9 million in fiscal year 2004 due to decreased loan activity.

Grant revenue recognized from the Federal and State governments totaled \$6.9 million in fiscal year 2004, an 38.8% decrease from fiscal year 2004 due to decreased loan activity.

Loans made totaled \$4.8 million during the year, which represents an decrease of \$4.5 million from the previous year. This is an decrease of 48.3% because of decreased new applications and draws on existing loans from municipalities and others through the State.

Loan collections (principal and interest) totaled \$1.1 million during the fiscal year. This represents an overall increase of \$0.9 million, or 430% from the prior year because more loan recipients had completed their projects, at which time repayments are required to take place.

Statement of Net Assets

The combined total net assets of the Fund for year ending June 30, 2005 increased by \$5.7 million or 32.5%. The following condensed statement of net assets shows a summary of changes in dollars and percentages between fiscal years.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS (Cont'd.)  
JUNE 30, 2005

TABLE 1  
NET ASSETS  
(Thousands of Dollars)

	<u>2005</u>	<u>2004</u>	<u>Increase (decrease)</u>	<u>Percent Change</u>
Cash	\$ 7,144.4	\$ 5,662.0	\$ 1,482.4	26.2
Receivables				
Loans, current portion	539.1	298.9	240.2	80.4
Loan interest	291.6	187.7	103.9	55.4
Loan to Drinking Water Grant Fund	891.1	-	891.1	100.0
Federal grant	601.7	1,753.1	(1,151.4)	65.7
State grant	<u>3,271.1</u>	<u>3,168.3</u>	<u>102.8</u>	<u>3.2</u>
Total current assets	12,739.0	11,070.0	1,669.0	15.1
NONCURRENT ASSETS				
Loans, net of current portion	<u>18,375.1</u>	<u>14,916.4</u>	<u>3,458.7</u>	<u>23.2</u>
Total assets	<u>\$31,114.1</u>	<u>\$25,986.4</u>	<u>\$ 5,127.7</u>	<u>19.7</u>
LIABILITIES				
State advances	\$ 601.7	\$ 1,753.1	\$ (1,151.4)	(65.7)
Accounts payable	-	2.1	(2.1)	(100.0)
Deferred revenue – state match	<u>7,339.6</u>	<u>6,743.8</u>	<u>595.8</u>	<u>8.8</u>
Total liabilities	7,941.3	8,499.0	(557.7)	(6.6)
NET ASSETS – unrestricted	<u>23,172.8</u>	<u>17,487.4</u>	<u>5,685.4</u>	<u>32.5</u>
Total liabilities and net assets	<u>\$31,114.1</u>	<u>\$25,986.4</u>	<u>\$ 5,127.7</u>	<u>19.7</u>

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS (Cont'd.)  
JUNE 30, 2005

Cash increased \$1.5 million (or 26.2%) to \$7.1 million as funds received from grants, including state matches were disbursed for loans. Loans receivable increased by \$3.7 million or 24.3% to \$18.9 million, mostly as a result of the issuance of seven new loans and more draws on existing loans. Federal grants receivable decreased by \$1.2 million or 65.7% mostly due to increased draw activity as of June 30, 2005.

State advances increased identically to Federal grants receivable as this account represents amounts advanced to the Fund in anticipation of Federal grants as of June 30, 2005. Deferred revenue from the State match increased \$0.6 million or 8.8% as the State appropriated additional funds from its 21<sup>st</sup> Century Fund to meet its future matching requirements against the capitalization grants awarded by the EPA.

Statement of Revenue, Expenses and Changes in Net Assets

The following schedule summarizes the statement of revenue, expenses and changes in net assets of the Fund for the fiscal years ended June 30, 2005 and 2004.



STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS (Cont'd.)  
JUNE 30, 2005

TABLE 2  
CHANGES IN NET ASSETS  
(Thousands of Dollars)

	<u>2005</u>	<u>2004</u>	<u>Increase (decrease)</u>	<u>Percent Change</u>
Operating revenue				
Loan origination fees	\$ 135.5	\$ 100.7	\$ 34.8	34.6
Interest income - loans	<u>593.1</u>	<u>372.1</u>	<u>221.0</u>	<u>59.4</u>
Total operating revenue	728.6	472.8	255.8	54.1
Operating expenses				
Salaries and related benefits	525.4	532.9	(7.5)	(1.4)
Contract services	292.6	309.4	(16.8)	(5.4)
Indirect costs	64.7	58.1	6.6	11.5
Subgrants	1,074.1	896.3	177.8	19.8
Supplies	50.4	50.6	(0.2)	(0.4)
Equipment	6.5	2.6	3.9	142.6
Travel	6.1	7.9	(1.8)	23.0
Training	<u>8.5</u>	<u>0.7</u>	<u>7.8</u>	<u>1,114.3</u>
Total operating expenses	<u>2,028.3</u>	<u>1,858.5</u>	<u>169.8</u>	<u>9.2</u>
Operating loss	(1,299.7)	(1,385.7)	86.0	6.2
Non-operating revenue				
Interest income – cash deposits	107.5	97.2	10.3	10.3
Grant Revenue	3,782.3	7,308.9	(3,526.6)	(48.3)
Grant Revenue - set asides	2,030.5	1,858.5	172.0	9.3
State Match	<u>1,064.8</u>	<u>2,062.5</u>	<u>(997.7)</u>	<u>(48.4)</u>
Total non-operating revenue	<u>6,985.1</u>	<u>11,327.1</u>	<u>4,342.0</u>	<u>(38.3)</u>
Change in net assets	5,685.4	9,941.4	(4,256.0)	(42.8)
Net assets, beginning of year	<u>17,487.4</u>	<u>7,546.0</u>	<u>9,941.4</u>	<u>131.7</u>
Net assets, end of year	<u>\$23,172.8</u>	<u>\$17,487.4</u>	<u>\$ 5,685.4</u>	<u>32.5</u>

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS (Cont'd.)  
JUNE 30, 2005

Federal grant revenue decreased by \$3.5 million or 48.3% and the State match decreased by \$1.0 million or 48.4 % both mostly as a result of the decrease in demand from municipalities for the low-interest loans during the current year.

Federal grant revenue for set-aside sub-funds increased by \$0.2 million or 9.3% due to increased activities in the set-aside sub-funds.

Operating expenses increased by \$0.2 million or 9.2 % due mainly to increased activity in the sub-funds and the removal of the State-wide hiring freeze.

## FINANCIAL STATEMENTS

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
STATEMENTS OF FUND NET ASSETS  
JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>2004</u>
<b>CURRENT ASSETS</b>		
Cash	\$ 7,144,385	\$ 5,661,981
Loans receivable - current portion	539,101	298,859
Loan interest receivable	291,535	187,713
Loan from Drinking Water Grant Fund	891,050	-
Federal grants receivable	601,728	1,753,054
State grants receivable	<u>3,271,120</u>	<u>3,168,320</u>
Total current assets	12,738,919	11,069,927
<b>NONCURRENT ASSETS</b>		
Loans receivable - net of current portion	<u>18,375,140</u>	<u>14,916,408</u>
Total assets	<u><u>\$ 31,114,059</u></u>	<u><u>\$ 25,986,335</u></u>
<b>CURRENT LIABILITIES</b>		
State advances	\$ 601,728	\$ 1,753,054
Accounts payable	-	2,100
<b>LONG-TERM LIABILITIES</b>		
Deferred revenue - state match	<u>7,339,627</u>	<u>6,743,816</u>
Total liabilities	7,941,355	8,498,970
<b>NET ASSETS - unrestricted</b>	<u>23,172,704</u>	<u>17,487,365</u>
Total liabilities and net assets	<u><u>\$ 31,114,059</u></u>	<u><u>\$ 25,986,335</u></u>

The accompanying notes are an integral part of these statements.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
STATEMENT OF REVENUE, EXPENSES AND CHANGES IN FUND NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
<b>OPERATING REVENUE</b>		
Interest income - loans	\$ 296,576	\$ 186,047
Interest income - administrative fees	296,575	186,047
Loan origination fees	135,497	100,665
	<hr/>	<hr/>
Total operating revenue	728,648	472,759
 <b>OPERATING EXPENSES</b>		
Salaries and related benefits	525,365	532,919
Contract services	292,647	309,406
Indirect costs	64,736	58,060
Subgrants	1,074,104	896,259
Supplies	50,389	50,573
Equipment	6,508	2,683
Training	8,500	700
Travel	6,110	7,934
	<hr/>	<hr/>
Total operating expenses	2,028,359	1,858,534
 Operating loss	(1,299,712)	(1,385,775)
 <b>NON-OPERATING REVENUE</b>		
Interest income - cash	107,480	97,217
Grant revenue	3,782,302	7,308,878
Grant revenue - set asides	2,030,459	1,858,534
State match	1,064,809	2,062,521
	<hr/>	<hr/>
Total non-operating revenue	6,985,050	11,327,150
 <b>CHANGE IN NET ASSETS</b>	5,685,339	9,941,375
 Net assets, beginning of year	<hr/> 17,487,365	<hr/> 7,545,990
 Net assets, end of year	<hr/> <u>\$ 23,172,704</u>	<hr/> <u>\$ 17,487,365</u>

The accompanying notes are an integral part of these statements.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
STATEMENTS OF CASH FLOWS  
YEARS ENDED JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities		
Loan repayments	\$ 1,148,137	\$ 216,002
Interest received from borrowers	489,329	292,135
Loan origination fees	135,497	100,665
Loan disbursements	(4,847,111)	(9,371,398)
Salaries and related benefits paid	(525,365)	(532,919)
General expenses paid	<u>(1,505,094)</u>	<u>(1,323,515)</u>
Net cash used by operating activities	(5,104,608)	(10,619,030)
Cash flows from investing activities		
Interest received from cash deposits	<u>107,480</u>	<u>97,217</u>
Net cash provided by investing activities	107,480	97,217
Cash flows from noncapital financing activities		
Loan to Drinking Water Grant Fund	(891,050)	-
Grants received from EPA	6,964,087	7,585,258
Advances from State of Delaware	(1,151,326)	1,582,154
Grants received from State of Delaware	<u>1,557,820</u>	<u>-</u>
Net cash provided by noncapital financing activities	<u>6,479,531</u>	<u>9,167,412</u>
CHANGE IN CASH AND CASH EQUIVALENTS	1,482,404	(1,354,401)
Cash and cash equivalents - beginning of year	<u>5,661,981</u>	<u>7,016,382</u>
Cash and cash equivalents, end of year	<u>\$ 7,144,385</u>	<u>\$ 5,661,981</u>
Cash flows from operating activities		
Operating loss	\$ (1,299,712)	\$ (1,385,775)
Adjustments to reconcile net income to net cash provided by operating activities		
Loans receivable	(3,698,974)	(9,155,396)
Increase in interest receivable	(103,822)	(79,959)
Accounts payable	<u>(2,100)</u>	<u>2,100</u>
Net cash used by operating activities	<u>\$ (5,104,608)</u>	<u>\$ (10,619,030)</u>

The accompanying notes are an integral part of these statements.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2005

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

This summary of significant accounting policies of the State of Delaware Drinking Water Revolving Loan Fund (the Fund) is presented to assist in understanding the Fund's financial statements. The financial statements and notes are representations of the Fund's management which is responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America and have been consistently applied in the preparation of the financial statements.

**General Background.** The State of Delaware Drinking Water Revolving Loan Fund established through Chapter 79, Title 29, Subsection 15 of the Delaware Code, provides financial assistance to eligible public water systems in Delaware for the planning, design and construction of drinking water facilities as well as loans for land acquisition for source water protection purposes. The Fund is funded through federal capitalization grants as established under Section 1452 of the Safe Drinking Water Act. The Act requires the State of Delaware to provide matching funds equal to 20 percent of federal funds received.

Standard loans made by the Fund must be repaid within 20 – 30 years. All repayments, including interest and principal, must remain in the Fund.

The Fund is administered by the State of Delaware, Department of Health and Social Services (DHSS), Division of Public Health (DPH) under the supervision of the Governor's Cabinet Committee on State Planning Issues. DPH's primary activities include making loans, providing direct assistance and managing the coordination of the Fund to meet the objectives of the Safe Drinking Water Act. In the year ended June 30, 1999, Congress authorized the Environmental Protection Agency (EPA) to award \$12,558,800 in Federal Fiscal Year 1997 grants to the State of Delaware. Delaware committed \$2,511,760 (20% match) to the program, meeting its state match requirements (Notes 8 and 10). This grant was closed in fiscal year 2005. In the year ended June 30, 2001, Congress authorized EPA to award \$14,585,100 in Federal Fiscal Year 2000 grants to the State of Delaware. Delaware committed \$2,917,020 (20% match) to the program, meeting its state match requirements (Note 8). In the year ended June 30, 2002, Congress authorized EPA to award \$7,757,000 in Federal Fiscal Year 2001 grants to the State of Delaware. Delaware committed \$1,551,400 (20% match) to the program, meeting its state match requirement, which was deposited by the state into the Fund during fiscal year 2003. A fourth award was given in the year ended June 30, 2003 when Congress authorized EPA to award \$7,789,100 in Federal Fiscal Year 2002 grants to the State of Delaware. Delaware committed \$1,557,820 (20% match) to the program, meeting its state match requirement. A fifth award was given in the year ended June 30, 2004 when Congress authorized EPA to award

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2005

**SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd.)**

\$8,052,500 in Federal Fiscal Year 2003 grants to the State of Delaware. Delaware committed \$1,610,500 (20% match) to the program, meeting its state match requirement. A sixth award was given in the year ended June 30, 2005 when Congress authorized EPA to award \$8,303,100 in Federal Fiscal Year 2004 grants to the State of Delaware. Delaware committed \$1,660,620 (20% match) to the program, meeting its state match requirements. The fourth award was deposited by the State into the Fund during fiscal year 2005. The fifth and sixth awards will be deposited by the State into the Fund during fiscal year 2006.

The Fund is accounted for as an enterprise fund. The Fund is made up of several sub-funds, each of which is considered a separate accounting entity. The sub-funds are described below:

Loan Fund

The primary purpose of the Loan Fund is to serve as a permanent loan fund to make low-interest loans to public water systems.

Set-aside Sub-Funds

The set-aside funds are used to account for the proceeds of specific grant revenues that are legally restricted to expenditures for specific purposes.



STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2005

**SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd.)**

Set-aside Sub-Funds (Cont'd.)

There are four such funds.

1. The 2% Technical Assistance Sub-Fund is used to account for the funds allotted to the State (up to 2% of the total) to provide assistance to public water systems serving 10,000 people or fewer.
2. The 4% Administration Sub-Fund is used to account for the funds allotted to the State (up to 4% of the total) for the reasonable costs of administering the programs under section 1452 and providing technical assistance. These costs may include such activities as issuing debt; program start-up costs; audit costs; financial, management and legal consulting fees; development of an intended use plan and priority ranking system; development of affordability criteria; and cost of support services provided by other State agencies.
3. The 10% Program Management Sub-Fund is used to account for the funds allotted to the State (up to 10% of the total) to:
  - a. administer the State Public Water Supply System (PWSS) program;
  - b. administer or provide technical assistance through source water protection programs;
  - c. develop and implement a capacity development strategy; and
  - d. develop and implement an operator certification program.

The State must provide a dollar for dollar match (100 percent for up to 10 percent of the capitalization grant) for capitalization grant funds used for these purposes. This match is separate, and in addition to, the 20 percent match for the capitalization grant.

4. The 15% Local Assistance Sub-Funds are used to fund several other categories of activities to assist development and implementation of local drinking water protection initiatives with the stipulation that not more than 20% of the capitalization grant amount can be used for any one activity.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2005

**SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd.)**

**Type of Entity and Division of Funds.** The Fund's activities are accounted for as a distinct operating unit within the DPH. Accordingly, the financial statements of the Fund are intended to present the financial position and the results of operations of only that portion of the funds and account groups of the State of Delaware that is attributable to the transactions of the Fund.

**Adoption of GASB Statement 20.** The Fund has adopted the provision of GASB Statement 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting", which provides for the consistent application or nonapplication to proprietary funds of pronouncements of the Financial Accounting Standards Board (FASB), issued after November 30, 1989. Accordingly, the Fund has elected not to adopt FASB pronouncements issued after November 30, 1989, unless GASB specifically adopts such pronouncements.

**Basis of Accounting.** The Fund uses the economic resources measurement focus and the accrual basis of accounting. Revenue is recognized when earned and expenses are recognized when the liability is incurred.

**Recognition of Revenues.** By the terms of agreements between the State and the EPA, federal assistance provided to the Fund is earned when qualified loans and expenditures are made to eligible public water systems. Matching funds provided by the State are considered earned by the same criteria. However, the State's matching requirement for the Set-aside Funds was met using designated expenditures made for other programs; therefore, no State monies were required to be provided to the Set-aside Funds. The State's matching requirement for the Loan Fund was made using State General Fund monies.

Amounts earned in excess of grant monies received from EPA and the State are recorded as grants receivable, whereas an excess of grant monies received over the amounts earned is recorded as deferred grant revenue. A right of set-off does not exist between the State and EPA.

**Cash and Cash Equivalents.** For purposes of the statement of cash flows, the Fund considers short-term investments with an original maturity of three months or less to be cash equivalents.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2005

**SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd.)**

**Operating and Non-operating Revenues.** The Fund considers revenue from its lending activities in the Loan sub-fund to be operating. It considers revenue from grants and interest income received on cash deposits to be non-operating.

**Use of Estimates.** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**NOTE 2 CASH**

**Cash:** "Cash" as reported on the statement of net assets represents the Fund's allocated share of cash, cash equivalents and investments under the control of the Treasurer of the State of Delaware. All cash deposited with the Treasurer by state agencies is maintained by the Treasurer in various pooled funds. The State Treasurer invests the deposited cash including cash float in short-term securities and other investments. However, the Fund may deposit or withdraw cash at any time without prior notice or penalty. Interest income is credited to the Fund based on the weighted average rate of return on the State's monies applied to the Fund's average daily cash balance. The classification of pooled cash and investments of the Fund is not determinable at the entity level. Pooled investments represent those investments in units of a pool rather than specific securities. As a result, such investments are not categorized as to risk because they are not evidenced by securities that exist in a physical or book-entry form.

**The Cash Management Policy Board:** The Corporation follows the "Statement of Objectives and Guidelines for the Investments of State of Delaware", of the State's Cash Management Policy Board (the Board). The Board, created by State law, establishes policies for, and the terms, conditions, and other matters relating to, the investment of all money belonging to the State with certain limited exceptions.

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**CASH (Cont'd.)**

***Investment Guidelines and Management:*** The State's Cash Management Policy categorizes all cash and special purpose funds for which the State is financially accountable as follows:

- A. Cash Accounts: Divide the State's available cash into three parts:
  - 1) Collection and Disbursement Accounts,
  - 2) Cash and Liquidity Accounts,
  - 3) Reserve Cash (Intermediate) Accounts.
- B. Special Purpose Accounts. There are two primary types of Special Purpose Accounts:
  - 1) Endowment Accounts,
  - 2) Authority Accounts: The State's Authorities (State Agencies, Local School Districts and Component Units) maintain a variety of fund types, including various operating funds, bond funds and debt service reserve funds.

The Fund's accounts are considered Cash Accounts.

The investment guidelines, adopted by the Board provide, among other things, that no more than 10% of the entire portfolio may be invested in obligations of any one issuer other than the U.S. Government. Investments may be made only in fixed income instruments with maturities of up to five years in certain circumstances. The State's Cash Management Policy is available on the Internet at <http://www.state.de.us/treasure/information/cash.shtml>.

**Custodial Credit Risk**

***Collateralization Requirements:*** All State deposits are required by law to be collateralized by direct obligations of, or obligations which are guaranteed by, the United States of America, or other suitable obligations as determined by the Board, unless the Board shall find such collateralization not in the best interest of the State. The Board has determined that certificates of deposit and time deposits must be collateralized, unless the bank issuing the certificate has assets of not less than \$5 billion and is rated not lower than "B" by Fitch, Inc. Bank Watch. The Board has also determined that State demand deposits need not be collateralized provided that any bank that holds these funds has had for the last two years, a return on average assets of 0.5% or greater and an average equity-capital ratio of at least 1:20. If the bank does not meet the above criteria, collateral must consist of one or more of the following:

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**CASH (Cont'd.)**

- (a) U.S. Government securities;
- (b) U.S. Government agency securities;
- (c) Federal Home Loan Board letters of credit;
- (d) State of Delaware securities; or
- (e) Securities of a political subdivision of the State with a Moody's Investors Service rating of "A" or better.

Additionally, the bank must ensure that those securities pledged as collateral have a market value equal to or greater than 102% of the ledger balance(s) in the account(s) each day and ensure that securities pledged are identified as held in the State's name and are segregated on the bank's records.

At June 30, 2005, the financial institutions maintaining the Fund's deposits satisfied the criteria listed above and the deposits held by those institutions did not require collateralization.

**NOTE 3 AVAILABLE FUNDING, DISBURSEMENTS AND REMAINING BALANCE  
BY FUNDING YEAR**

As of June 30, 2005, the Fund had open federal grants totaling \$59,045,600, from which it had had made disbursements of \$25,746,678. The breakdown for all grants (except for the 2004 grant in the amount of \$8,303,100) is as follows. As of June 30, 2005, the 2004 grant had not been appropriated and no disbursement from it had yet been made.

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**AVAILABLE FUNDING, DISBURSEMENTS AND REMAINING BALANCE BY FUNDING YEAR (Cont'd.)**

**Loan Fund**

<u>Grant Year</u>	<u>Committed Portion of Available Funding</u>	<u>Disbursed to Date</u>	<u>Remaining Balance</u>
1997	\$ 9,288,036	\$ 9,288,036	\$ -
1999	10,184,089	3,018,653	7,165,436
2001	5,352,330	2,210,301	3,142,029
2002	5,653,979	1,535,731	4,118,248
2003	<u>5,712,775</u>	<u>-</u>	<u>5,712,775</u>
Total	<u>\$36,191,209</u>	<u>\$16,052,721</u>	<u>\$20,138,488</u>

**Set-aside Funds**

2% Technical Assistance

<u>Grant Year</u>	<u>Committed Portion of Available Funding</u>	<u>Disbursed to Date</u>	<u>Remaining Balance</u>
1997	\$ 251,176	\$ 251,176	\$ -
1999	291,702	291,702	-
2001	155,140	153,181	1,959
2002	155,782	35,036	120,746
2003	<u>161,050</u>	<u>3,008</u>	<u>158,042</u>
Total	<u>\$ 1,014,850</u>	<u>\$ 734,103</u>	<u>\$ 280,747</u>

4% Administration

<u>Grant Year</u>	<u>Committed Portion of Available Funding</u>	<u>Disbursed to Date</u>	<u>Remaining Balance</u>
1997	\$ 502,352	\$ 502,352	\$ -
1999	583,404	572,160	11,244
2001	310,280	253,308	56,972
2002	311,564	233,919	77,645
2003	<u>322,100</u>	<u>67,445</u>	<u>254,655</u>
Total	<u>\$ 2,029,700</u>	<u>\$ 1,629,184</u>	<u>\$ 400,516</u>

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**AVAILABLE FUNDING, DISBURSEMENTS AND REMAINING BALANCE  
BY FUNDING YEAR (Cont'd.)**

10% Program Management

<u>Grant Year</u>	<u>Committed Portion of Available Funding</u>	<u>Disbursed to Date</u>	<u>Remaining Balance</u>
1997	\$ 633,416	\$ 633,416	\$ -
1999	1,458,510	1,428,788	29,722
2001	775,700	729,353	46,347
2002	778,910	732,881	46,029
2003	805,250	454,416	350,834
Total	<u>\$ 4,451,786</u>	<u>\$ 3,978,854</u>	<u>\$ 472,932</u>

15% Local Assistance

<u>Grant Year</u>	<u>Committed Portion of Available Funding</u>	<u>Disbursed to Date</u>	<u>Remaining Balance</u>
1997	\$ 1,883,820	\$ 1,883,820	\$ -
1999	2,067,395	492,061	1,575,334
2001	1,163,550	350,147	813,403
2002	888,865	452,740	436,125
2003	1,051,325	173,048	878,277
Total	<u>\$ 7,054,955</u>	<u>\$ 3,351,816</u>	<u>\$ 3,703,139</u>

Total Program Balance

<u>Grant Year</u>	<u>Committed Portion of Available Funding</u>	<u>Disbursed to Date</u>	<u>Remaining Balance</u>
1997	\$12,558,800	\$12,558,800	\$ -
1999	14,585,100	5,803,366	8,781,734
2001	7,757,000	3,696,290	4,060,710
2002	7,789,100	2,990,306	4,798,794
2003	8,052,500	697,916	7,354,584
Total	<u>\$50,742,500</u>	<u>\$25,746,678</u>	<u>\$24,995,822</u>

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**NOTE 4 UNUSED FEDERAL FUNDS**

The following is a summary of the federal cash draws and disbursements executed during fiscal year 2005 and the remaining unused balance for the 1997, 1999, 2001, 2002 and 2003 entitlements as of June 30, 2005:

	1997 <u>Entitlement</u>	1999 <u>Entitlement</u>	2001 <u>Entitlement</u>	2002 <u>Entitlement</u>	2003 <u>Entitlement</u>
Beginning balance	\$ -	\$ -	\$ -	\$ -	\$ -
Federal grant payments	3,225,336	516,474	689,831	1,966,034	598,488
Loan disbursements	(2,589,181)	(519,721)	(543,982)	(129,418)	-
Set aside disbursements	(636,155)	3,247	(145,849)	(1,836,616)	(598,488)
Unused federal funds	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

**NOTE 5 GRANTS RECEIVABLE**

Grants receivable of \$601,728 and \$1,753,054 as of June 30, 2005 and 2004, respectively, represent amounts due from the Federal government for amounts expended or accrued.

**NOTE 6 LOANS RECEIVABLE**

The loans receivable account is made up of the following major categories.

	<u>Binding Commitments</u>	<u>Loans Receivable</u>	
		<u>2005</u>	<u>2004</u>
Artesian Water Company, Fenwick Island and South Bethany	\$ 4,307,144	\$ 3,800,384	\$3,953,277
Town of Frankford	820,000	779,391	820,000
Town of Felton	370,000	303,927	318,659
Town of Blades #1	401,300	378,370	389,921
Town of Milton	643,370	635,621	519,673
Town of Greenwood	932,000	60,919	60,919
J.H. Wilkerson & Son, Inc. – Broadkill I	270,800	252,526	261,849
J.H. Wilkerson & Son, Inc. – Broadkill II	140,000	96,128	98,673
Tidewater Utilities, Inc. #1	783,647	769,238	374,775



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**LOANS RECEIVABLE (Cont'd.)**

	<u>Binding Commitments</u>	<u>Loans Receivable</u>	
		<u>2005</u>	<u>2004</u>
Granada Mobile Home Park	34,321	28,687	31,497
City of Wilmington	11,000,000	860,909	566,342
Artesian Water Company #2	2,900,285	1,412,549	2,245,768
Tidewater Utilities #2	3,274,418	2,357,224	1,640,879
Town of Dagsboro	839,519	839,519	167,830
Artesian Water Company #3	5,456,495	2,222,960	1,971,415
Town of Smyrna	1,751,515	1,628,147	1,692,841
Town of Frankford #2	275,000	258,167	100,949
Town of Millsboro	893,200	586,683	-
Town of Laurel	1,083,000	533,487	-
City of Lewes	1,276,000	578,222	-
Tidewater Utilities #3	882,535	531,183	-
Town of Blades #2	212,780	-	-
City of Lewes #2	716,000	-	-
Town of Dagsboro #2	560,481	-	-
City of Wilmington #2	13,700,000	-	-
Tidewater Utilities #4	<u>2,000,000</u>	<u>-</u>	<u>-</u>
	55,523,810	18,914,241	15,215,267
Less: Current portion	<u>-</u>	<u>539,101</u>	<u>298,859</u>
	<u>\$55,523,810</u>	<u>\$18,375,140</u>	<u>\$14,916,408</u>

Interest charged on these loans ranges from 1.5% to 4.46%. Interest earned on loans receivable was \$593,152 and \$372,094 for the years ending June 30, 2005 and 2004, respectively.

Loan maturities vary based on individual agreements. General Obligation and Municipal Revenue Bonds are collateral for municipal loans; business assets and real estate are collateral for mortgage loans.

There is no allowance for doubtful accounts as of June 30, 2005 and 2004. As of June 30, 2005 and 2004, there were no material delinquent loan balances. There were no loan defaults for the years ended June 30, 2005 and 2004. There has been no history of significant bad debts or uncollectible accounts.

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**LOANS RECEIVABLE (Cont'd.)**

Binding Loan Commitments: The Fund has \$55,523,810 of current and future binding loan commitments as of June 30, 2005. EPA had set a binding commitment requirement of \$46,333,241 through June 30, 2005. The Fund is in compliance with EPA's requirement.

**NOTE 7 STATE ADVANCES**

The State advances of \$601,728 and \$1,753,054 as of June 30, 2005 and 2004, respectively, represent amounts advanced to the Fund by the State of Delaware's General Fund in anticipation of reimbursement from Federal grants.

**NOTE 8 DEFERRED REVENUE – STATE MATCH**

As of June 30, 2005, the Fund had total available state match funding in its separate cash account as follows:

<u>Grant Year</u>	<u>Committed Portion of Available Funding</u>	<u>Disbursed to Date</u>	<u>Remaining Balance</u>
1997	\$ 2,511,760	\$2,511,760	\$ -
1999	2,917,020	873,065	2,043,955
2001	1,551,400	317,020	1,234,380
2002	1,557,820	642,746	915,074
2003	1,610,500	124,902	1,485,598
2004	<u>1,660,620</u>	<u>-</u>	<u>1,660,620</u>
Total	<u>\$11,809,120</u>	<u>\$4,469,493</u>	<u>\$7,339,627</u>

Interest earned on cash deposits totals \$107,480 and \$97,217 for the years ending June 30, 2005 and 2004, respectively.

The State owes the Fund \$3,271,120 and \$3,168,320 at June 30, 2005 and 2004, respectively, for the committed portion of available funding, and these amounts are included in State grants receivable.

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**NOTE 9 PENSION**

Employees of the Fund are considered employees of the State of Delaware ("State") and are covered under The State Employees' Pension Plan. Total pension cost of \$48,831 for 2005 and \$44,208 for 2004 is included in the financial statements personnel costs. Certain significant plan provisions follow:

Detailed information regarding this plan is available in the Delaware Code and the Rules and Regulations of the Board of Pension Trustees.

Plan Description and Eligibility: The State Employees' Pension Plan is a cost-sharing multiple employer defined benefit plan that covers virtually all full-time or regular part-time employees of the State, including employees of other affiliated entities.

Service Benefits: Final average monthly compensation multiplied by 2.0% and multiplied by years of credited service prior to January 1, 1997 plus final average compensation multiplied by 1.85% and multiplied by years of credited service after December 31, 1996, subject to minimum limitations. For this plan, final average monthly compensation is the monthly average of the highest three years of compensation.

Vesting: Five (5) years of credited service.

Retirement: Age 62 with five (5) years of credited service; age 60 with 15 years of credited service; or after 30 years of credited service at any age.

Disability Benefits: Same as Service Benefits. Employee must have five (5) consecutive years of credited service.

Survivor Benefits: If employee is receiving a pension or is active with at least five (5) years of credited service, eligible survivor receives 50% (or 75% with 3% reduction of benefit) of the benefit the employee would have received at age 62.

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**PENSION (Cont'd.)**

Contributions:

- Employer - Determined by Board of Pension Trustees.
- Employee - 3 % of earnings in excess of \$6,000.

Death Benefit:           \$7,000 per member.

The Delaware Public Employees' Retirement System issues a publicly available financial report that includes financial statements and required supplementary information of the plan. The financial report may be obtained by writing to the State Board of Pension Trustees and Office of Pensions, McArdle Building, Suite #1, 860 Silver lake Boulevard, Dover, Delaware 19904-2402.

**NOTE 10 COMMITMENTS AND CONTINGENCIES**

General: The Fund is exposed to various risks of loss related to torts, thefts of assets, errors or omissions, injuries to state employees while performing Fund business, or acts of God.

The State maintains insurance for all risks of loss which is included in the indirect costs charged to the Fund. There have not been any claims against the Fund since its inception.

Lease: The State of Delaware, Department of Administrative Services (DAS), on behalf of the Fund, entered into an operating lease for the office space occupied by the Fund on September 17, 1999. Annual rental under the old lease was \$55,080 for the first year with 3% increases thereafter. The DAS agreed to execute a First Amendment and Extension of Lease on November 1, 2004. Annual rental under the new lease is \$63,113 per annum (\$5,259 per month).

The original lease was for a term of five years commencing November 1, 1999 and terminating October 31, 2004. The extension commenced November 1, 2004 and terminates April 30, 2006.

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**COMMITMENTS AND CONTINGENCIES (Cont'd.)**

Noncancellable future minimum lease payments under the lease as of June 30, 2005 are:

Years ending June 30

2006

\$52,594

**NOTE 11    LOAN TO DRINKING WATER GRANT FUND**

The Fund loaned \$891,050 during fiscal year 2005 to the State of Delaware, Department of Health and Social Services, Division of Public Health, Office of Drinking Water, Drinking Water Grant Fund (DWGF). This loan was made to assist DWGF's shortage of cash available to pay an obligation incurred during the fiscal year. DWGF will repay the Fund in full at no interest during fiscal year 2006.

## SUPPLEMENTARY INFORMATION

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
STATEMENT OF FUND NET ASSETS BY FUND  
JUNE 30, 2005

	Loan Fund	2% Technical Assistance	4% Admin- istration	10% Program Management	15% Local Assistance	Total
<b>CURRENT ASSETS</b>						
Cash	\$ 7,144,385	\$ -	\$ -	\$ -	\$ -	\$ 7,144,385
Loans receivable - current portion	539,101	-	-	-	-	539,101
Loan interest receivable	291,535	-	-	-	-	291,535
Loan from Drinking Water Grant Fund	891,050	-	-	-	-	891,050
Federal grants receivable	385,708	1,165	43,985	41,809	129,061	601,728
State grants receivable	3,271,120					3,271,120
Total current assets	12,522,899	1,165	43,985	41,809	129,061	12,738,919
<b>NONCURRENT ASSETS</b>						
Loans receivable - net of current portion	18,375,140	-	-	-	-	18,375,140
Total assets	<u>\$ 30,898,039</u>	<u>\$ 1,165</u>	<u>\$ 43,985</u>	<u>\$ 41,809</u>	<u>\$ 129,061</u>	<u>\$ 31,114,059</u>
<b>CURRENT LIABILITIES</b>						
State advances	\$ 385,708	\$ 1,165	\$ 43,985	\$ 41,809	\$ 129,061	\$ 601,728
<b>LONG-TERM LIABILITIES</b>						
Deferred revenue - state match	7,339,627	-	-	-	-	7,339,627
Total liabilities	7,725,335	1,165	43,985	41,809	129,061	7,941,355
NET ASSETS - unrestricted	<u>23,172,704</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>23,172,704</u>
Total liabilities and net assets	<u>\$ 30,898,039</u>	<u>\$ 1,165</u>	<u>\$ 43,985</u>	<u>\$ 41,809</u>	<u>\$ 129,061</u>	<u>\$ 31,114,059</u>

STATE OF DELAWARE  
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STATEMENT OF FUND NET ASSETS BY FUND  
JUNE 30, 2004

	Loan Fund	2% Technical Assistance	4% Admin- istration	10% Program Management	15% Local Assistance	Total
<b>CURRENT ASSETS</b>						
Cash	\$ 5,661,981	\$ -	\$ -	-	\$ -	\$ 5,661,981
Loans receivable - current portion	298,859	-	-	-	-	298,859
Loan interest receivable	187,713	-	-	-	-	187,713
Federal grants receivable	1,555,351	510	45,851	107,911	43,431	1,753,054
State grants receivable	3,168,320	-	-	-	-	3,168,320
 Total current assets	 10,872,224	 510	 45,851	 107,911	 43,431	 11,069,927
<b>NONCURRENT ASSETS</b>						
Loans receivable - net of current portio	14,916,408	-	-	-	-	14,916,408
 Total assets	 <u>\$ 25,788,632</u>	 <u>\$ 510</u>	 <u>\$ 45,851</u>	 <u>107,911</u>	 <u>\$ 43,431</u>	 <u>\$ 25,986,335</u>
 <b>CURRENT LIABILITIES</b>						
State advances	\$ 1,555,351	\$ 510	\$ 45,851	\$ 107,911	\$ 43,431	\$ 1,753,054
Accounts Payable	2,100	-	-	-	-	2,100
<b>LONG-TERM LIABILITIES</b>						
Deferred revenue - state match	6,743,816	-	-	-	-	6,743,816
 Total liabilities	 8,301,267	 510	 45,851	 107,911	 43,431	 8,498,970
 NET ASSETS - unrestricted	 17,487,365	 -	 -	 -	 -	 17,487,365
 Total liabilities and net assets	 <u>\$ 25,788,632</u>	 <u>\$ 510</u>	 <u>\$ 45,851</u>	 <u>\$ 107,911</u>	 <u>\$ 43,431</u>	 <u>\$ 25,986,335</u>



STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
STATEMENT OF REVENUE, EXPENSES AND CHANGES IN FUND NET ASSETS BY FUND  
FOR THE YEAR ENDED JUNE 30, 2005

	Loan Fund	2% Technical Assistance	4% Adminis- tration	10% Program Management	15% Local Assistance	Total
<b>OPERATING REVENUE</b>						
Interest income - loans	\$ 296,576	\$ -	\$ -	\$ -	\$ -	\$ 296,576
Interest income - administrative fees	296,575	-	-	-	-	296,575
Application fees	135,497	-	-	-	-	135,497
 Total operating revenue	 728,648	 -	 -	 -	 -	 728,648
 <b>OPERATING EXPENSES</b>						
Salaries and related benefits	-	7,039	90,049	252,998	175,279	525,365
Contract services	(2,100)	26,192	909	239,826	27,820	292,647
Indirect costs	-	791	9,410	36,625	17,910	64,736
Subgrants	-	-	106,398	224,755	742,951	1,074,104
Supplies	-	-	-	50,389	-	50,389
Equipment	-	-	-	6,508	-	6,508
Training	-	-	-	8,500	-	8,500
Travel	-	-	-	6,110	-	6,110
 Total operating expenses	 (2,100)	 34,022	 206,766	 825,711	 963,960	 2,028,359
 Operating income (loss)	 730,748	 (34,022)	 (206,766)	 (825,711)	 (963,960)	 (1,299,712)
<b>NON-OPERATING REVENUE</b>						
Interest income - cash	107,480	-	-	-	-	107,480
Grant revenue	3,782,302	-	-	-	-	3,782,302
Grant revenue - set asides	-	34,022	206,766	825,711	963,960	2,030,459
State match	1,064,809	-	-	-	-	1,064,809
 Total non-operating revenue	 4,954,591	 34,022	 206,766	 825,711	 963,960	 6,985,050
 <b>CHANGE IN NET ASSETS</b>	 5,685,339	 -	 -	 -	 -	 5,685,339
Net assets, beginning of year	17,487,365	-	-	-	-	17,487,365
Net assets, end of year	<u>\$23,172,704</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$23,172,704</u>

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
STATEMENT OF REVENUE, EXPENSES AND CHANGES IN FUND NET ASSETS BY FUND  
FOR THE YEAR ENDED JUNE 30, 2004

	Loan Fund	2% Technical Assistance	4% Adminis- tration	10% Program Management	15% Local Assistance	Total
<b>OPERATING REVENUE</b>						
Interest income - loans	\$ 186,047	\$ -	\$ -	\$ -	\$ -	\$ 186,047
Interest income - administrative fee	186,047	-	-	-	-	186,047
Loan origination fees	100,665	-	-	-	-	100,665
<b>Total operating revenue</b>	<b>472,759</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>472,759</b>
<b>OPERATING EXPENSES</b>						
Salaries and related benefits	-	3,764	86,517	380,540	62,098	532,919
Contract services	-	137,343	980	171,083	-	309,406
Indirect costs	-	258	10,388	43,079	4,335	58,060
Subgrants	-	-	135,086	200,832	560,341	896,259
Supplies	-	-	285	50,288	-	50,573
Equipment	-	-	-	2,683	-	2,683
Training	-	-	-	700	-	700
Travel	-	-	-	7,934	-	7,934
<b>Total operating expenses</b>	<b>-</b>	<b>141,365</b>	<b>233,256</b>	<b>857,139</b>	<b>626,774</b>	<b>1,858,534</b>
<b>Operating income (loss)</b>	<b>472,759</b>	<b>(141,365)</b>	<b>(233,256)</b>	<b>(857,139)</b>	<b>(626,774)</b>	<b>(1,385,775)</b>
<b>NON-OPERATING REVENUE</b>						
Interest income - cash	97,217	-	-	-	-	97,217
Grant revenue	7,308,878	-	-	-	-	7,308,878
Grant revenue - set asides	-	141,365	233,256	857,139	626,774	1,858,534
State match	2,062,521	-	-	-	-	2,062,521
<b>Total non-operating revenue</b>	<b>9,468,616</b>	<b>141,365</b>	<b>233,256</b>	<b>857,139</b>	<b>626,774</b>	<b>11,327,150</b>
<b>CHANGE IN NET ASSETS</b>	<b>9,941,375</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>9,941,375</b>
Net assets, beginning of year	7,545,990	-	-	-	-	7,545,990
<b>Net assets, end of year</b>	<b>\$ 17,487,365</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 17,487,365</b>

Independent Auditors' Report on Internal Control Over  
Financial Reporting and on Compliance and Other  
Matters Based on an Audit of the Financial Statements  
in Accordance with Government Auditing Standards

To the Management  
Drinking Water Revolving Loan Fund  
State of Delaware

We have audited the financial statements of the State of Delaware Drinking Water Revolving Loan Fund (the Fund) as of and for the year ended June 30, 2005, and have issued our report thereon dated January 26, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Fund's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Delaware Drinking Water Revolving Loan Fund's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely

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Independent Auditors' Report on Internal Control Over  
Financial Reporting and on Compliance and Other  
Matters Based on an Audit of the Financial Statements  
in Accordance with Government Auditing Standards (Cont'd.)

Internal Control Over Financial Reporting (Cont'd.)

period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

This report is intended for the information of the Fund's management, Environmental Protection Agency, Office of Auditor of Accounts, Office of the Governor, Office of the Controller General, Office of Management and Budget, Office of the Attorney General and the Department of Finance and is not intended to be used and should not be used by anyone other than these specified parties. However, under 29Del.C., Section 10002(d), this report is a public record and its distribution is not limited.

*McBride, Shopa & Co*

Wilmington, Delaware  
January 26, 2006

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FISCAL YEAR ENDED JUNE 30, 2005

**CURRENT YEAR FINDINGS**

None.

STATE OF DELAWARE  
DRINKING WATER REVOLVING LOAN FUND  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FISCAL YEAR ENDED JUNE 30, 2005

**CURRENT STATUS OF PRIOR YEAR FINDINGS**

**FINDING 02-01:** The implementing regulations of the Safe Drinking Water Act (40 CFR Part 35, Subpart L) require that cumulative binding commitments be made in an amount equal to the amount of each federal grant award plus the required state match, within one year of the receipt of each grant award. The level of loans EPA expects the Fund to execute \$24,923,543 in loans for the period March 31, 2002 through June 30, 2005.

The Fund has not executed enough loans to meet the binding commitment requirement as set by EPA (\$24,923,543 threshold vs. \$8,620,335 executed), thus, the Fund is not in compliance with this requirement.

WE RECOMMEND THAT more loans be executed or that the Fund communicate with EPA to extend the period of time to meet the binding commitment requirement.

**AUDITEE'S PLAN FOR CORRECTIVE ACTION:**

The City of Wilmington signed a Binding Commitment letter on July 9, 2002 and closed a \$11 million loan on August 23, 2002 for the Cool Springs Reservoir project.

The Town of Greenwood signed a Binding Commitment letter on July 24, 2002 and closed a \$932,000 loan on October 20, 2000.

We will continue to attempt to close loans to be in compliance.

**CURRENT STATUS:**

Binding commitments reached \$55,523,810 at June 30, 2005, which is above EPA's required level. Therefore, this is no longer a finding.